SUMMARY of COOPERATIVE CASES

FARM CREDIT ADMINISTRATION
U. S. DEPARTMENT OF AGRICULTURE
WASHINGTON, D. C.

SUMMARY NO. 55

DECEMBER 1952

UNITED STATES DEPARTMENT OF AGRICULTURE
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Prepared for the

COOPERATIVE RESEARCH AND SERVICE DIVISION

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Comments on accounting-economic aspects of tax cases by

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COOPERATIVE RESEARCH AND SERVICE DIVISION

Summary No. 55 December 1952

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The comments on cases reviewed herein represent the personal opinion of the authors and not necessarily the official views of the Department of Agriculture.

NONEXEMPT COOPERATIVE LEGALLY OBLIGATED TO PAY PATRONAGE REFUNDS MAY EXCLUDE SUCH REFUNDS FROM ITS GROSS INCOME

(Otsego County Cooperative Association, Inc., v. C.I.R.)

The Tax Court of the United States on July 31, 1952, rendered its decision in the case of Otsego County Cooperative Association, Inc., Petitioner, v. Commissioner of Internal Revenue, Respondent, Docket No. 28479.

The petitioner is a cooperative association organized under the laws of Michigan to operate as a farmers' cooperative, and to engage in the marketing of farm products and the purchase and distribution of farm production supplies. It paid patronage refunds to its patrons during the taxable years 1946, 1947, and 1948, and excluded the amount of such refunds from its gross income. The respondent denied the exclusions on the ground that the petitioner was not legally obligated to make the payments and that therefore such amounts were income to the cooperative. The Court held that the association was legally obligated to make such payments and that the payments should be excluded in computing the association's net income subject to tax.

Excerpts from the facts stated by the Court, pertinent to the question as to whether the association was legally obligated to pay patronage refunds, are as follows:

> "The methods used by petitioner in the receipt and disposal of revenues were governed by Article VIII of the By-Laws.
>
> "Section 4 of that Article provides:
>
> > "The corporation is authorized to deduct and retain from sales proceeds of agricultural products or supplies or charges for services such amounts are deemed necessary and adequate for expenses, including provision for depreciation and other valuation reserves, interest on indebtedness, and for all capital purposes including capital reserves and surpluses required or permitted by law, and such other amounts as shall be necessary for furth [sic] capitalization of the corporation.
>
> "Section 5 of the Article provides for the disposition of amounts retained during the year for capital purposes, as follows:
>
> > "At the close of each fiscal year amounts retained during the year for capital purposes and amounts deducted from sales proceeds or charges for services in excess of amount required for expenses, including provision for depreciation and other valuation reserves and for interest on indebtedness, shall be distributed upon a patronage basis as revolving fund credits to the patrons delivering the products, purchasing supplies or receiving services from the corporation.

"Section 6 of the Article, which relates to the allocation to patrons of general reserves, is as follows:

> "The books and records of the corporation shall be kept in such manner, by years, that the amount retained and carried to general reserves accruing from the patronage of each patron, stockholder and non-stockholder, is allocated to each separately.
>
> "Whenever in a given year the operation of the corporation results in a net loss, such loss, to the extent that general reserves are available, shall be charged against the same and they shall be thereby reduced accordingly. The board of directors shall prescribe the basis [sic] on which the reserve contributions of patrons by years shall be reduced on account of any such loss, so that it will be borne on as equitable basis as the board of directors finds practical.
>
> "Whenever in the discretion of the board of directors the reserves are found to be in excess of the amount deemed reasonably necessary for the sound financial operations of the corporation, such excess shall be applied to paying off ratably, by years, the oldest unexhausted reserve contribution of patrons.
>
> "Upon dissolution or winding up of the corporation in any manner, after the payment of all debts, including revolving certificates of indebtedness, and the retirement at par of all outstanding capital stock, any balance remaining shall be distributed ratably on an equitable basis to those who have patronized and are patronizing the corporation.

"Section 7 of the Article, which relates to stockholders' equities, is as follows:

> "This corporation shall be operated without profit. The financial interest of the stockholders shall be that of creditors of the corporation. Stockholders, as such, shall have no interest in any capital reserve or surplus but such interest shall be vested in the patrons in proportion to their contribution to the aggregate capital reserves of the corporation. Stockholders shall not be entitled to dividends on capital stock nor shall payment of dividends on capital stock be permitted.

"Section 8 of the Article provides that patronage credits of nonmember patrons who are eligible for membership (farmers) shall be applied to the purchase price of one share of capital stock; whereupon, the status of such nonmember patron is converted to that of a member patron.

"Section 9 of the Article, which provides for a revolving fund method of financing, is as follows:

> "It is the purpose of this corporation that its entire capital will be supplied eventually by its patrons in proportion to their patronage.
>
> "The following program for financing is adopted to provide a plan under which each patron will furnish capital for financing the corporation in the approximate proportion that they patronize the corporation and for which capital the corporation will issue revolving certificates of indebtedness as evidence of the indebtedness owned by it to its patrons for the capital so furnished by them and for retiring such revolving certificates of indebtedness.
>
> "Patronage divident [sic] credits allocated to patrons whose total credits issued in that year do not exceed the sum of $3.00 may be paid in cash when in the judgment of the board of directors it appears advisable to so do. Otherwise, patronage dividend credits allocated to patrons shall not be paid in cash but shall be credited to patrons to be issued as revolving certificates of indebtedness, provided, however, the first Ten ($10.00) dollars of revolving fund credits issued to each non-stockholder patron eligible to become a stockholder shall be applied as payment for a share of capital stock.

"Section 10 of the Article, which relates to revolving certificates of indebtedness, is as follows:

> "The board of directors shall have authority to issue revolving certificates of indebtedness of an unlimited amount for use in connection with the revolving plan of financing the corporation.

"These certificates shall contain the following priorities, conditions, and requirements, but otherwise shall be in such form as shall be approved by the board of directors:

> "(1) The claims of holders of revolving certificates of indebtedness of account thereof shall be junior to the claims of all other creditors but shall have priority over all claims of capital stock.
>
> "(2) Revolving certificates of indebtedness may be issued in any denomination or principal amount of one ($1.00) dollar or more.
>
> "(3) Revolving certificates of indebtedness shall be numbered consecutively and issued in their consecutive numerical order.

"(4) Revolving certificates of indebtedness shall be freely transferable, provided however, that any certificate offered for transfer must be returned to the corporation for cancellation, transfer of title and reissue of a new certificate, provided further, that the certificate to be reissued shall bear the same number as the certificate surrendered for transfer.

"(5) Revolving certificates of indebtedness shall bear only such rate of interest as the board of directors may stipulate, provided, that such rate of interest shall in no event exceed a rate of five (5%) per cent per annum upon the principal amount of the revolving certificates of indebtedness outstanding, providing further, that interest at the rate of five (5%) per cent per annum shall be paid upon the principal amount of revolving certificates of indebtedness outstanding before any distribution of earnings is made to patrons upon a patronage basis. Interest upon revolving certificates of indebtedness shall not be cumulative if unpaid. Interest paid upon any revolving certificate of indebtedness shall be paid ratably upon all revolving certificates of indebtedness outstanding except those which have been called for payment and have not been surrendered in accordance with the call therefor.

"(6) Revolving certificates of indebtedness shall not carry a fixed maturity date but shall contain provision by which the board of directors shall have power to call and retire any amount or all the outstanding revolving certificates of indebtedness as and when in their judgment the corporation shall have cash funds available for the purpose, provided further, outstanding revolving certificates of indebtedness shall be called in their consecutive numerical order of issue, the oldest outstanding revolving certificates of indebtedness having priority in their call for payment, except in the event of the death of the holder of revolving certificates of indebtedness, in which event the board of directors may, in its own discretion, authorize the retirement[sic] of the revolving certificates of indebtedness held by such deceased holder before the normal order of their retirement on the basis of their numerical order of issue.

"Petitioner's certificates of indebtedness were assignable and transferable as shown by the following paragraph which was included therein:

"This certificate is transferable only on the books of this corporation upon surrender of the certificate properly endorsed and when any indebtedness owed to the corporation by the owner hereof has been fully paid. Upon transfer of ownership of title

to the claim represented hereby and surrender of this certificate for transfer and reissue, this certificate shall be cancelled and the certificate issued shall bear the same numerical number as the certificate surrendered for transfer.

"The bookkeeping procedure observed by petitioner with respect to allocation of patronage refund credits each fiscal year was described by petitioner's accountant as follows:

> "After a computation of the total amount of patronage dividends is made, the amount is credited to the capital stock credit account or the reserve for patronage dividends--it's the same--and then when the stock is issued and the certificates of indebtedness are issued, the charge is made to that account and credited to either capital stock outstanding or certificates of indebtedness outstanding.
>
> "The procedure used by petitioner for distributing income at the end of the taxable years was as follows: The profit and loss account was debited with the amount which the board of directors decided was to be placed in the reserve for patronage refunds account and a credit made to this latter account. When the board of directors decided that certificates of indebtedness should be issued, the amount decided upon was debited to the reserve for patronage refunds account and a credit was made to the certificates of indebtedness account. Certificates were then issued to the stockholder patrons. If a patron was not yet a stockholder, his credit in the reserve for patronage refunds was withheld until such time as the par value of a share of capital stock ($10) had accrued, at which time a share of stock was issued to him. When the board of directors decided that the certificates of indebtedness were to be redeemed, a debit was made to the certificates of indebtedness account for the amount determined and a credit was made to the cash account."

The memorandum opinion of Judge Rice is set forth below in its entirety:

> "Before we consider the issue presented, it seems pertinent to point out that no question of exemption under section 101 (12) of the Internal Revenue Code is involved, since the parties have stipulated that petitioner has not and does not claim to be exempt thereunder. Nor does petitioner claim any deduction under section 23 (a) of the Code; it rests its entire case upon the proposition that its patronage refunds constitute exclusions from gross income.
>
> "Whether petitioner is entitled to exclude from its gross income patronage refunds issued in the form of certificates of indebtedness and capital stock during the taxable years in

question depends upon whether the right of petitioner's patrons to such refunds arose by reason of an existing legal obligation prior to the actual receipt of such earnings by petitioner. If petitioner was legally required to make such a distribution, such earnings are not income to it and, consequently, are to be excluded in the computation of its net taxable income. Colony Farms Cooperative Dairy, Inc., 17 T.C. 688 (1951); United Cooperatives, Inc., 4 T.C. 93 (1944).

"The Michigan corporation statute, under which petitioner was incorporated, provides that cooperatives shall make distribution of surplus earnings on a patronage basis but that certain reserves of such earnings could be set up for future operations or future distribution, and that earnings so reserved must be allocated on the books of the cooperative or a means provided for such allocation for the stockholders or members or other persons entitled to such earnings before distribution of earnings is authorized and made.[1]

"During the taxable years in question, petitioner's By-Laws (Article VIII) authorized the retention by petitioner from its income such amounts 'as are deemed necessary and adequate for expenses, including provision for depreciation and other valuation reserves, interest on indebtedness, and for all capital purposes including capital reserves and surpluses required or permitted by law'. Any excess over expenses, including depreciation, reserves, and interest 'shall be distributed upon a patronage basis as revolving fund credits to the patrons delivering the products, purchasing supplies or receiving services from the corporation'.

"This Article also provides for allocation of patronage credits to the account of each patron with respect to the retained reserves. It provides that the amount of reserves shall be subject to diminution in case of operating losses; and for retirement of capital reserve credits upon the revolving fund plan, whenever the board of directors determines that accumulated capital reserves are adequate for operating capital. Payment of dividends on capital stock is prohibited and stockholders have no interest, direct or contingent, in the capital reserves. Each patron's capital credits are required to be evidenced by revolving fund certificates.

"We are of the opinion, after a careful study of the Michigan statute and the provisions of petitioner's Articles and By-Laws, that petitioner was under a preexisting legal obligation to pay patronage refunds, and that this case falls within the ambit of Colony Farms Cooperative Dairy, Inc., supra, and United Cooperatives, Inc., supra, and we so hold. See also Dr. P. Phillips Cooperative, 17 T.C. 1002 (1951). Petitioner is entitled to exclude from gross income for the taxable years the

[1]Chapter 195, § 21.100, Michigan Statutes Annotated.

> aggregate amount of $15,816.52 representing the certificates of indebtedness and capital stock issue in payment of patronage credits and the refund credit of $18.29 which was applied to petitioner's liens for debts. Since the record does not disclose the exact amounts allocable to each taxable year--
>
> Decision will be entered under Rule 50."

This case is another significant reaffirmation of the principle that when a cooperative makes payments of patronage refunds pursuant to a legal obligation such amounts are not income to the cooperative and should be excluded in computing the cooperative's net income subject to corporate tax. The decision also throws further light on what the Court regards as an adequate legal obligation as the basis for such exclusion.

(R. J. Mischler)

A number of Tax Court decisions, both recently and in the past, have affirmed the principle described by Mr. Mischler. One wonders in the face of this why the Otsego case was ever brought to trial. I have a feeling the issue hinged on the fact that the Commissioner of Internal Revenue probably contended the wording of the legal papers did not constitute a clear and valid obligation to distribute patronage refunds, in which contention the Court did not concur.

This is certainly an outstanding example of how carefully worded the legal papers must be if an association wants to avoid difficulties with the taxing authorities.

In this instance the association was of the non-tax-exempt type. However, the new regulations proposed by the Commissioner of Internal Revenue on November 8, 1952 to govern the tax treatment of the so-called exempt cooperatives (those coming under Section 101(12) of the Internal Revenue Code) carry the stipulation that patronage dividends which an association desires to treat as a reduction of its taxable income must be made "in fulfillment and satisfaction of a valid obligation of such association to the patron, which obligation was in existence prior to the receipt by the cooperative association of the amount allocated...."

Thus, if the new regulations are finally adopted as now proposed, the exempt group of cooperatives will do well to give greater attention to the preciseness with which their legal papers are worded.

The references in this case to "the profit and loss account" of the association and to its "earnings" reflect a lack of appreciation of the true character of a cooperative operation. In such an operation the dealings with members and other patrons do not produce a profit or an earning. Indeed, if a particular amount ever had the status of an earning it could not change its nature and become an exclusion from income, as decided by the Court.

(George J. Waas)

COOPERATIVE ORDERED TO STOP PRICE DISCRIMINATIONS

(In Re Florida Citrus Canners Cooperative)

Florida Citrus Canners Cooperative, of Lake Wales, Florida, has been ordered by the Federal Trade Commission to cease and desist from unlawfully discriminating in price as between competing purchasers of its canned citrus fruit juice products. The order (Docket No. 5640, issued July 14, 1952) also binds the cooperative's officers, members and agents.

The respondents' pricing practice of charging some of their customers higher prices for products of like grade and quality than the prices charged competing customers was found by the Commission to have been in violation of the Clayton Antitrust Act, as amended by the Robinson-Patman Act (Subsection (a) of section 2).

According to the Commission's findings, the recipient of the cooperative's discriminatory prices was the Great Atlantic & Pacific Tea Company, whose constituent units are described as "the largest purchasers and retailers of grocery products within the United States." In one canning season, the findings state, the A & P chain received discriminatory price benefits aggregating approximately $600,000 on purchases of about 750,000 cases of "Donald Duck" brand citrus fruit juice products.

Finding that the effect of the prices differences amounting to 1.5 percent or more of the higher prices was to substantially lessen competition in the sale and distribution of citrus fruit juices, the Commission said:

> "The discriminatory prices at which said products were offered for sale, sold and distributed by Florida Citrus Canners Cooperative to The Great Atlantic & Pacific Tea Company system as above described enabled said system to retail 'Donald Duck' labeled citrus fruit juice products at a decided sales price advantage over other retailers selling Florida Citrus Canners Cooperative's products of like grade and quality in competitive resale in the areas concerned."

As a basis for its order prohibiting price differences generally in the sale of its products of like grade and quality to customers engaged competitively in the resale of such products, the Commission concluded that:

> ". . . any substantial discrimination in price, including discriminations smaller than 1.5% of the higher price, in the sale of fruit juice products, may have the same or substantially the same competitive effect."

All of the Commissioners except Chairman Mead, who did not participate, concurred in the decision after consideration of the record, including the respondents' objections to a tentative order the Commission had

previously issued setting forth the terms of an order to cease and desist it proposed to issue after making appropriate findings as to the facts and conclusion.

(R. J. Mischler)

FEDERAL TRANSPORTATION TAX

(Gulf Coast Towing Company v. United States)

The United States Court of Appeals, 5th Circuit, decided a case on May 16, 1952, involving Federal transportation taxes, which may be of interest to cooperatives involved in transportation. The case is Gulf Coast Towing Company v. United States, 196 F. 2d 944.

Section 3475(a) of the Internal Revenue Code, insofar as it is relevant to the case under consideration, imposes upon the amount paid for transportation of property by rail, motor vehicle, water, or air from one point in the United States to another a tax equal to 3 percent of the amount so paid. This tax applies only to amounts paid to a person engaged in the business of transporting property for hire.

One of the problems in applying this provision of the statute has been to determine when a person is "engaged in the business of transferring property for hire." Obviously, if a person transports property which he owns (has title to), he is not transporting property for hire. Moreover, if he makes a bona fide lease of transportation equipment and transports therein property which he owns, he is not engaged in transporting property for hire. A number of borderline cases can arise, however, where the facts are not as clear. This case deals with one such factual situation.

In this case, a towing company contracted with a cement corporation to furnish a tug and tow-barges for six months in consideration of a fixed daily rate, which was to be paid by the cement corporation whether the tug and crew were used on a particular day or not. The towing company agreed to maintain a complete crew on the tug and to furnish all stores, fuels, oils, tow-lines, and to take care of all other expenses connected with the operation of the tug. The towing company was to carry insurance on the tug at its own expense and agreed to assume all liability for damage of property by third parties or injuries to third persons or members of the crew or tug or tow, or both. While the cement corporation furnished all sailing directions, the detailed navigation of the tug or tow was under control and direction of the captain of the tug, who was in the employ of the towing company. After reviewing these facts, the Court held that the contracts in question were contracts for the transportation of property and not merely a lease or charter of the tug, and hence that the towing company was subject to the transportation tax.

The following excerpts from the Court's opinion disclose the reasoning of the Court:

> "Appellant urges that the trial Court erred in finding that it was engaged in the transportation of property for hire within the meaning of the statute, insofar as the transactions described are concerned. Although stated variously, the crux of the contention is that the contracts were not contracts for transportation of property, but were contracts for rental, lease or charter of marine equipment under which Lone Star Cement Corporation transported its own property by use of the leased tug. It is contended on behalf of appellee that the question can not be so limited since, under the facts of this case, the contractual agreement was specifically one for towage and otherwise provided a transportation service.
>
> "The same question here presented, arising from substantially the same facts, was determined by the District Court in Ohio River Sand Co. v. United States, 60 F. Supp. 563. In that case the Court recognized that the towing of barges constituted transportation, but held, as the appellant contends here, that the transaction evidenced a lease of the tugboat on a rental basis so that the lessee could transport its own property, and that the lessor was compensated for rental as the owner of the tug and was not engaged in the business of transporting property for hire'. In Bridge Auto Renting Corp. v. Pedrick, 174 F. 2d 733, 737, the Court of Appeals for the Second Circuit referred to the Ohio River Sand Company case, supra, as being 'indistinguishable', but expressly declined to follow it. The Bridge Auto Renting Corporation case decision involved a business where the taxpayer leased trucks to business concerns for hauling purposes and, as immediately there involved, the situation where the lessor furnished 42 of the taxpayer's customers drivers as well as trucks. The Court found these drivers to be employees of the taxpayer and, one judge dissenting, concluded that the lessor was engaged in the business of transporting property for hire as to such trucks. That decision turned upon the Court's answer to the questions stated, that the 'lessor' furnished 'substantially all the facilities for and perform[ed] substantially all of the functions of, transporting the property of the * * * customers whose payments to it were taxed'. This Court has recently had occasion to reiterate that the existence of tax liability under the statute now involved 'depends upon whether the transaction in question in any case is "transportation" within the terms of the statute. This is generally a question of fact * * *.' Masonite Corp. v. Fly, 5 Cir., 182 F. 2d 934, 935; Masonite Corp. v. Fly, 5 Cir., 194 F. 2d 257, 261. In the second appearance of the case it was emphasized that the intent of the statute 'was to tax amounts paid to a person "engaged in the business of transporting property for hire".'
>
> "Upon our consideration of the facts presented to us we conclude, contrary to the result reached by the Court in the Ohio River Sand Company case, supra, that the amounts upon which the tax was paid

were 'paid to a person engaged in the business of transporting property for hire'. There can be no question that the compensation received by the towing company was that for the operation of a fully manned tugboat for towing barges, loaded and unloaded, used by the cement corporation in transporting raw materials used in its cement manufacturing business. Both the barges and the raw materials loaded thereon and towed by appellant's tug under the towage agreement were the 'property' of the cement corporation. Such towage was the transportation of property. As we view the contracts the performance of the towage contract was the obligation of the appellant and its compensation was received by virtue of its engagement in the business of transporting property for hire. Under the terms of the contract, and the means and method of operations thereunder the arrangement did not evidence a transportation by the cement corporation. The terms of the contract and the method of operation thereunder require the conclusion that the appellant was in fact furnishing transportation to the cement corporation, whose payments to it were taxed, and did not merely lease or charter a tug. For the consideration paid appellant furnished the tug and crew and performed the towing service. While the cement corporation furnished the sailing directions, the master of the tug was at all times an employee of appellant and was responsible for the detailed navigation of the tug. Appellant was liable for any damages or injuries inflicted in operating the tug and was also responsible for any injuries sustained by members of the crew of the tug and/or tow. A different result is not required because of the fact that the amount paid for the towage services was fixed at a daily rate, and was to be paid whether the tug and its crew were used on a particular day or not. The statute is not concerned with the method used to compute the amount of the payment. Such amount, however it may be computed, is taxable, if, in legal effect, it is paid for transportation. The obvious purpose of the agreement to pay whether or not the tug was engaged in the towing operation on a particular day was to insure the availability of the tug at all times when towage might be desired.

"The contracts in question were contracts for transportation of property for hire and the compensation paid therefor was taxable. We have considered appellant's contention that the Lone Star Cement Corporation, by virtue of the contract, became owner of the tug, pro hac vice, under admiralty law, but find it without merit. The judgment of the trial Court is affirmed."

(R. J. Mischler)

TAX COURT RULES AGAIN THAT CONTRIBUTIONS TO NATIONAL TAX EQUALITY ASSOCIATION ARE NOT DEDUCTIBLE FOR INCOME TAX PURPOSES

(American Hardware & Equipment Co. v. C.I.R.)

A decision was entered on June 24, 1952, by the Tax Court of the United States in the case of American Hardware & Equipment Co., Petitioner, v. Commissioner of Internal Revenue, Respondent, Docket No. 29793, holding that amounts of $1,800 and $1,500 contributed by the petitioner in the respective taxable years 1947 and 1948 to the National Tax Equality Association, an exempt corporation organized and primarily operated in those years for the carrying on of propaganda with the ultimate objective being a revision in the tax structure, were not properly deductible under either Section 23 (a) (1) (A) or 23 (q) (2) of the Internal Revenue Code. The decision of the Tax Court was in the form of a memorandum opinion by Judge LeMire. The effect of the decision is that the American Hardware & Equipment Company of North Carolina will have to pay an income tax on the $3,300 contributed to NTEA in 1947 and 1948. The amount of the tax appears as slightly less than $1,000.

The Court pointed out in the opinion that the sole issue presented in the case was whether the amounts contributed by the American Hardware & Equipment Company to NTEA constituted proper deductions under either of the cited sections of the Internal Revenue Code. The Court observed that the identical question had been passed upon in the Roberts Dairy Company case, which decision of the Tax Court was affirmed on appeal on April 15, 1952, by the Circuit Court of Appeals for the Eighth Circuit. (See Summaries No. 49, page 8, and No. 54, page 7.) In reliance upon the decision in that case, which found NTEA to be organized and primarily operated for the carrying on of propaganda to influence legislation, the Court held that the contributions to NTEA were not deductible for income tax purposes.

(R. J. Mischler)

PAYMENTS TO COOPERATIVES BY HANDLERS UNDER FEDERAL MILK ORDER

(Babcock Dairy Company v. Brannan)

Babcock Dairy Company v. Brannan, Civil Action No. 6668 in the District Court of the United States for the Northern District of Ohio, Western Division, Toledo, Ohio, was argued orally on October 23, 1952. At conclusion of the argument the court delivered an informal oral opinion and ruled that the provision of the Toledo, Ohio, Milk Order requiring milk handlers to pay directly to a cooperative association for milk delivered by persons from whom such association had written authorization to collect such payments is invalid. The case was remanded to the Secretary with directions to delete the provision in question.

The Judge observed that the record indicated to him that the handlers purchased their milk directly from the producers, not from the association of producers. Accordingly, he expressed the view that under section 608c(5)(B)(i), 7 U.S.C., there was no authority for a provision in the milk order for payment to anyone other than the producers, since the Act states that the Order may provide for the following provisions "and no other":

> "(i) for the payment to all producers and associations of producers delivering milk to the same handler of uniform prices for all milk delivered by them . . ."

Also, the court indicated that the orders should contain only matters that may be pertinent to the establishment and maintenance of parity prices and orderly marketing conditions.

Findings of Fact and Conclusions of Law were filed on November 13, 1952. Among the findings of fact were the following:

> "15. The marketing conditions are and have been for the last ten years orderly and stable in the Toledo Milk Marketing Area. The evidence affirmatively establishes this condition to be true.
>
> "16. At least parity prices have been established and maintained in the Toledo Milk Marketing Area for the last ten years. The evidence establishes this fact without question.
>
> "17. The handlers have paid their producers promptly and accurately for all milk purchased from the producers during the existence of the Federal Milk Marketing Order No. 30. The evidence affirmatively establishes this fact.
>
> * * * * * *
>
> "20. The conditions and circumstances surrounding the industry indicate that the market will remain orderly and stable.
>
> "21. There has been no blending of producers' milk by the cooperative association in the past in this milk marketing area and there is no intention to do so in the future. The testimony of the then manager of the cooperative establishes this fact.
>
> "22. The Northwestern Cooperative Association does not actually take title to the producers' milk nor is the producers' milk transferred to the Association nor does the Association acquire the milk from the producers.
>
> "23. The producers through their agents, the haulers, deliver their milk to the handler and the milk is acquired and purchased by the handler from the producers. Title passes directly from the producers to the handler. There is no actual consignment of the milk to the association.

"24. The association has no full supply agreement with the handlers nor does it have an agreement to relieve the handlers of the burdensome surplus that occurs throughout the year.

"25. The association of producers has no facilities to accept delivery of milk from its member producers or any other producers in the Milk Marketing Area.

"26. The handlers seek and acquire the producers."

The Conclusions of Law were as follows:

"1. The Court has jurisdiction of the parties in this cause and the subject matter thereof. (Subsection 15(B) of Section 8(c) of the Agricultural Adjustment Act of 1933, as amended and reenacted and amended by the Agricultural Marketing Agreement Act of 1937 7 U.S.C.A. 608c(15)(B).)

"2. The declaration of policy in the Agricultural Adjustment Act of 1933 and the Agricultural Marketing Agreement Act of 1937 states that it is the purpose of Congress to provide machinery whereby orderly marketing conditions for agricultural commodities in interstate commerce, including milk in this case, may be maintained, so that parity prices for agricultural commodities will be established.

"3. Since the Toledo Milk Marketing Area has been orderly for the past ten years, and since there is no evidence in the record of any threat of disorder or chaos, which would adversely affect parity prices, the Secretary of Agriculture is without statutory authority under the aforesaid act to promulgate the amendments in question.

"4. Section 608 c(5) of the Agricultural Adjustment Act provides that orders issued by the Secretary of Agriculture in the case of milk and its products shall contain certain terms and conditions, 'and no others.' The amendments promulgated by the Secretary of Agriculture in this case are not included in the terms and conditions specified in that section. Said amendments, therefore, are outside the statutory authority given by Congress to the Secretary of Agriculture.

"5. Under section 610(b)(1) associations of producers may be permitted to act as agents for their members in connection with the distribution of payments made by handlers for milk. That section is permissive only and does not authorize the Secretary of Agriculture to impose a mandatory requirement upon handlers to make payments for such milk to an association, and thus render it unlawful for said handlers to make payments directly to the producers from whom they purchase and take deliveries of milk.

"6. Section 610(b)(1) of the aforesaid act authorizing the Secretary of Agriculture to encourage cooperatives does not enlarge the scope

of the authority delegated to the Secretary of Agriculture by the Congress. That authority is limited to the promulgation of orders necessary to bring about stability and orderliness in milk marketing conditions, and thereby maintain parity prices for milk.

"7. Section 608(c)(7)(D) which authorizes the Secretary to include terms in his orders 'incidental to, and not inconsistent with the terms and conditions specified in subsections (5), (6) and (7) and necessary to effectuate the provisions of such order,' does not justify the Secretary's action in this case, since the provisions of the order here involved are inconsistent with section 608 c(5), which, in the case of milk, prohibits the Secretary from including in his orders any terms other than those specified therein. The terms of this order are not included in the specific terms and conditions there set forth.

"8. Since the Secretary's order is without authority under either the specific provisions of the statute or the 'necessary or incidental' provisions, the Court, by virtue of the authority set forth in section 608 c(15)(B) herewith remands these proceedings to the Secretary of Agriculture to delete the amendments to Order No. 30 numbered 930.7(a), 930.7(b) and 930.2(c)(10)."

(R. J. Mischler)

NEW REGULATIONS PROPOSED TENTATIVELY NOVEMBER 8, 1952 BY COMMISSIONER OF INTERNAL REVENUE TO GOVERN THE INCOME TAX TREATMENT OF EXEMPT COOPERATIVES AND THE PATRONS OF ALL COOPERATIVES

On November 8, 1952 the Commissioner of Internal Revenue, by publication in the Federal Register, proposed the making of rules connected with the income tax treatment of cooperatives which are qualified for inclusion under Section 101(12) of the Internal Revenue Code. Such rules also cover the manner in which patrons shall include patronage dividends, refunds and rebates in their own tax returns.

Those desiring to read the Commissioner's proposed regulations, which are of considerable importance to farmers' marketing and purchasing cooperatives, may refer either to the Federal Register for November 8, 1952 or to Supplement No. 2 to Miscellaneous Report 156 issued by the Farm Credit Administration, Washington 25, D. C. on November 8, 1952.

The proposal is subject to change before final adoption. The Commissioner will give consideration to any data, views, or arguments pertaining to this proposal which are submitted to him in writing in duplicate before December 9, 1952. The address is Commissioner of Internal Revenue, Washington 25, D. C.

(George J. Waas)